INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE, IT & MANAGEMENT

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    RESULTS & DISCUSSION
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PAYMENTS BANKS: A NEW LANDSCAPE FOR INDIAN BANKING SECTOR

ANUSHA GOEL
RESEARCH SCHOLAR
DEPARTMENT OF COMMERCE
FACULTY OF COMMERCE & BUSINESS
DELHI SCHOOL OF ECONOMICS
UNIVERSITY OF DELHI
DELHI

ABSTRACT
Payments Banks present an exciting opportunity for digital financial inclusion in India. Present article provides information about what are payments banks, various guidelines issued by RBI and issues involved in its operation. This article has been written after gathering information from sources like newspapers and RBI website. Several countries like Japan, South Africa, Brazil have created such institutions years ago. Now RBI has initiated for the development of similar institutions which is a welcoming step. But the successful applicants should keep in mind the challenges mentioned here and are willing to learn from the experiences of mobile money in other countries.

KEYWORDS
Banking, Payments Bank, Prepaid Instrument Providers, Telecom Sector.

JEL CODE
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INTRODUCTION
Financial inclusion has emerged as one of the initiatives over the past few years. In terms of outcomes, the overall experience is mixed. Despite opening large numbers of bank accounts, majority of them remain dormant because appropriate products were not offered to address the needs of the newly included population. According to the NSSO 59th Round Survey results 51.4% of farmer households are excluded from formal as well as informal sources of finance. Only 27% of the farm households access formal sources of credit while 73% have no access.

In the first phase of inclusion a number of different channels have emerged. Microfinance institutions (MFI), Business correspondents (BCs) and Prepaid Instrument Providers (PPI) have acted as a bridge between banks and newly included population by offering low cost services at the doorstep of customers. Telecom companies also provide low-cost remittance facilities using their networks. A feature shared among all these models is that they finance their operations either from equity or borrowings from banks.

The next phase of the process would be to combine the efficiencies of various channels with low-cost funds. This is what a payments bank will be. The main function will be to accept deposits from the public which will be fully covered by deposit insurance and invest the proceeds in government securities thus protecting them from any credit risk. So far the Indian banking sector is highly regulated with stiff entry barriers. May be the time has come to shed this cautious approach and taking a more liberal approach if inclusive growth is the objective.

BACKGROUND
Even globally, similar innovations have taken place and even gone further than they have in India. In 2007 the EU adopted the Payment Services Directive (PSD) to create a new group of payment service providers called “payment institutions” , especially to offer payment or remittance services without being a bank and do not include the entire range of services provided by a bank. In Japan, non-banks are allowed to provide funds transfers .South Africa permits non-banks to become clearing system participants and have full access to the clearing system subject to meeting the Central Bank’s requirements.

In Brazil, law creates a new legal entity known as a 'payments institution,' which would be supervised by the Brazilian Central Bank . Prepaid card issuers, digital wallet providers and telcos are eligible to apply for the license of payments institution with the minimum capital requirement of 2 million Brazilian Real. They were granted access to the clearing and settlement facilities operated by Central Bank and required to comply with simplified KYC procedures meant for low-value pre-paid payment accounts.

Given all these developments, any financial inclusion strategy would be ineffective if it did not create a room for independent non-bank participation to provide payment and deposit services.

WHAT IS PAYMENTS BANKS
This design is similar to a recently introduced class of companies called pre-paid instrument providers (PPIs) who can accept cash deposits from customers, credit them to an electronic “wallet” and allow to pay for goods and services. Currently they are permitted to accept a maximum amount of Rs.50,000 per customer and are required to deposit the aggregate amount with a scheduled commercial bank in an escrow account . Presently there are 27 PPIs authorised by the RBI under the Payment and Settlements Act, 2007. However there are certain issues involved with current model of prepaid instrument providers as follows:

1. KYC ISSUES

PPIs have been provided relaxed KYC requirements for their customers .Any transaction upto Rs. 50,000 can be undertaken on a wallet and restricting cash withdrawals from the wallets to banking outlets alone.

2. CUSTOMER AUTHENTICATION

In order to minimize risk and fulfill KYC norms, Aadhaar can play an important role in this regard but there are three issues- one that every access point for authentication and transaction represents an additional investment of Rs. 15,000 ; two, given that about 50 percent of the population do not possess Aadhaar cards and that there are entire states such as Chhattisgarh and Madhya Pradesh which have low penetration ; and three, biometric authentication may not be feasible in the most remote parts of the country given the slow roll-out of broadband and GPRS.

3. SAVINGS PRODUCT DESIGNS AND PAYMENT OF INTEREST

Currently PPIs are not allowed to pay interest on the wallet balances held by them. Even PPIs do not earn interest on their deposits with the sponsor bank and hence their ability in turn to pay interest also would be constrained.

4. CONTAGION RISK

There are concerns about the safety of funds being held by the PPIs since the amounts held with the sponsor bank are at risk and therefore do not enjoy the benefit of deposit protection

PAYMENTS BANK

Given these significant concerns of the PPI model regarding KYC norms, inability to pay interest on balances and contagion risk; and taking into account the urgent need to provide basic financial services like payment, deposit etc, it has been recommended that a set of banks may be licensed under the Banking Regulation Act, which may be referred to as Payments Banks.

Payments banks are "niche" or "differentiated" banks with the common objective of achieving financial inclusion. They will provide a limited range of products such as accepting demand deposits and remittances of funds to migrant workforce, low income earners, small businesses and unorganized sector entities through a widespread network in rural and unbanked areas. The basic functions like account opening formalities, service charges, facilities like cheque book, passbook and other paper based products will be same as that of commercial banks .

Key features of the Payments Banks are:

I) ELIGIBLE PROMOTERS

- The entities who can apply for Payments Bank license include existing non-bank Pre-paid Instrument Issuers (PPIs), Non-Banking Finance Companies (NBFCs), corporate BCs, mobile telephone companies, super-market chains, companies, real sector cooperatives , public sector entities and resident individuals having experience of atleast ten years in banking and finance.
- A promoter can have a joint venture with an existing scheduled commercial bank to start a payments bank.
- While evaluating the applicants, the Reserve Bank of India will consider the factors such as past record of sound credentials and integrity; financial soundness and successful track record of at least five years in running their businesses.

II) SCOPE OF ACTIVITIES

- Acceptance of demand deposits provided a balance of not more than Rs. 1,00,000 is maintained
- Issuing ATM/debit cards but cannot issue credit cards.
- Payments and remittance services through various channels including foreign remittances.
- Payment banks can offer locker and vault services
- Offering simple financial products like mutual fund units and insurance products etc.
- Can act as BC of another bank subject to meeting RBI guidelines
- Payment banks are prohibited from accepting deposits from NRIs

It can utilize the infrastructure of promoter provided there is an explicit agreement and customer confidentiality is maintained.

III) DEPLOYMENT OF FUNDS

- The payments bank cannot give short or long term loans to the public
- Along with maintaining Cash Reserve Ratio (CRR) with the Reserve Bank, it will be required to invest minimum 75 per cent of its "demand deposit" in specified Statutory Liquidity Ratio (SLR) securities with maturity of up to one year and the balance in an account with other scheduled commercial banks.

IV) CAPITAL REQUIREMENT

- The minimum capital required for payments banks shall be Rs. 100 crore. They would be required to satisfy capital adequacy requirements for both market risk and operations risk.
- The payments bank should have a leverage ratio of not less than 3 per cent

V) PROMOTER'S CONTRIBUTION

The promoter shall contribute atleast 40% of the initial capital for the first five years from the commencement of its business. Thereafter the shareholding can be reduced in a phased manner.

VI) FOREIGN SHAREHOLDING

Foreign investors can invest as per the Foreign Direct Investment (FDI) policy for private sector banks as amended from time to time.

HURDLES FOR A PAYMENTS BANK TO CROSS

In order to be successful, there are several issues that a payments bank has to address which are as follows:

India's cash addiction - People have preference for cash even in urban areas where alternatives exist. The 2014 Intermedia Financial Inclusion Insights (FII) survey of 45,000 Indian adults found that 82% of adults consider cash to be the "best tool" for small- to medium- transactions .

The over-the-counter (OTC) trap - Payments Banks might fall in "the OTC trap" i.e. the customer does not have an account but hands over cash to an agent who then facilitates the transaction from his account. It can become difficult to shift customers to account-based transactions. Further there will be usage through the payment account, but it cannot be termed as financial inclusion.

Competition from Banks - Retail fee income is one area where banks have increased their focus to accelerate their growth. It comprises commissions from sale of third-party products such as insurance and mutual funds, transaction charges on savings and current accounts, processing fees on consumer loans and credit cards, and fees from remittances. Payment Bank will face competition in the bill payments and prepaid card segment of PSBs

Low-cost domestic remittance alternatives- India already have low cost alternatives available where the average cost to make a domestic remittance across all channels was only 3.5% as compared to that of India Post (6%), informal sources (4.6%) and banks (3.0%). Payments Banks will need to offer their domestic transfer services at competitive prices.

Interest on deposits - The major source of revenue would comprise of fees and income from treasury operations. As a result, they are not in a position to offer interest rate of more than 4% on savings bank accounts which is already offered by most existing lenders. Therefore, it might not be easy to attract deposits.

Huge investment and long Payback period – To develop agent network large investments are required and it will take 3-5 years to generate low margins of around 2-5%.

Association with banks – They may not be able to attract customers by offering payment services alone so they require partnerships with credit-issuing banks.

CURRENT SCENARIO IN INDIA

Reserve bank of India has received a total of 41 applications for the Payments Bank license. Business entities have sought few clarifications regarding the structuring definition and FDI (foreign direct investment) and FII (foreign institutional investment) limits and branch policy. More clarity is required as to what constitute a branch. Some of the prominent names who have applied for license are given below.

India's largest lender - the State Bank of India has partnered with the country's largest company , Reliance Industries (RIL) to apply for a payments bank licence. SBI will hold 30% stake in the joint venture while RIL will be the promoter and hold the balance 70%. Vodafone has filed an application with the Reserve Bank of India for a payments bank licence. It being a subsidiary of UK parent Vodafone Group Plc needs a local partner. Vodafone's payment banking experience in Africa and Asia might give it a leg up among applicants. A Kenyan telecom operator partly owned by Vodafone i.e. Safaricom is widely considered as the biggest success story of mobile banking in developing countries. Aditya Birla Nuvo in partnership with the country's no 3 mobile phone operator , Idea Cellular has applied for a Payments Bank license. Aditya Birla Nuvo will hold 51% while Idea will hold the balance 49% in Idea Payments Bank Ltd. if a license is granted. Kotak Mahindra Bank has tied up with Bharti Airtel which already offers a wallet service named "Airtel Money". Further Bharti Airtel is having a network of 13 lakh touch points in about 50 million villages and covers 87 per cent of the total population.

Kishore Biyani-promoted Future Group has applied with the Reserve Bank of India. The company's physical presence in 168 cities across the country and rural locations in Gujarat and Punjab will help reach the depositors that include women, self-employed people as well as farmers and local entrepreneurs. If the license is issued, it will partner with IDFC bank. Suvidhaa Infoserve Ltd has joined the race by applying to RBI for payment bank licence. It is the flagship company of the Rs 6,500-crore e-commerce group Suvidhaa which is the largest non-bank entity offering domestic remittance service and other payment services in India. It has a footprint of 80,000 touch points across the country catering to over 28 million unique customers annually. ITZ Cash, an Essel Group company is another applicant. It is currently offering prepaid cards in association with IDBI Bank, DCB and HDFC Bank . It allows the under-served to make bill payments, shop online or by phone and cash withdrawals at ATMs without having a bank account. Bank of India will partner with You-First Money Express Private Limited, an entity promoted by former Citi Banker to apply for the license.

A Committee comprising of professionals from various fields like bankers, chartered accountants, financial analyst etc. will evaluate the applications. The final decision shall be taken by RBI.

A question arises as to why major telecom players like Airtel, Vodafone, Idea Cellular, Reliance are particularly interested in a payments bank license when it will involve huge investments and primarily cater to low income segment of the population ??

The answer is that its a game of small money, big business .Telecom companies are eyeing a sizable chunk of the additional revenue of Rs 14,000 crore from transaction fees, primarily from the remittances and cash-outs and cash-ins un-banked customers undertake on their payments bank accounts. They are planning to levy a fee of 2-3% which will come down with number of transactions, thus providing a margin of about 1% only.

Statistics suggest that there are about 180 million un-banked households with a corpus of Rs 4,32,000 crore .It is estimated that they will spend about Rs 18,000 annually, an overall amount of Rs 3,24,000 crore a year. It is only on this money that telcos can charge transaction fees. Even by charging three per cent, their revenue will turn out to be Rs 10,000 crore. Another area telcos will focus is fee from remittances which is estimated to be Rs 200,000-crore market mainly dominated by informal sector and not being reflected in official numbers (on remittances through India Post, mobile wallets, etc). Charging 2% fee will fetch them a revenue of Rs.4000 crore. They will even pay high interest i.e.7.5-8 per cent on deposits to attract investors.

In short, welfare gains will accrue from the last-mile delivery channels by achieving lower costs. So one would hope that all the current last-mile players irrespective of their business, would be eager to expand their scale of operations by opening payment banks.

CONCLUSION

The payments-bank model is potentially an important innovation, which will help increase the scale and efficiency of the financial inclusion process. There are several concerns raised about the viability of the Payments Bank as large profitable banks are offering payment services in a big way. It is highly unlikely that the payment bank business would be their main thing, which raises doubts about the intentions of business entities. Evidence also suggests that classroom learning and teaching interest rates will not change financial behavior. But opportunity still remains as existing banks have neglected people in providing small remittance facilities on account of the high costs and glamorous interiors. This innovation can prove successful only if proportionate regulations are applied and entities' core business interests are fully aligned with the inclusion objective, in terms of both products and delivery mechanisms. Awareness building has to be fused with the product that gets a change in behavior Investment in information technology is going to be key for service quality and efficiency. CRISIL Research and other experts suggest that telecom operators are ideal candidates to set up payments banks given their customer base and distribution networks in rural areas so RBI should consider this fact while taking final decision.

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